

Terry E. Branstad
Governor

Kim Reynolds
Lt. Governor



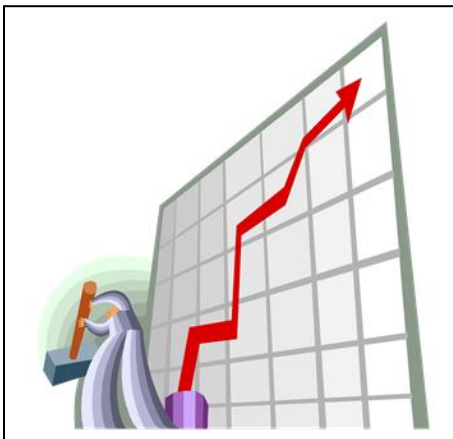
Terry Rich
Chief Executive Officer

Iowa Lottery Report On Operations

To: Members of the House Government Oversight Committee and Senate Government Oversight Committee

From: Terry Rich, CEO

Date: June 2013



We lead off this semi-annual report on lottery operations with some extremely positive news: **The Iowa Lottery will achieve record results in sales, proceeds to state causes, and prizes to players in its current fiscal year.**

Through the end of May, the latest month for which the lottery has complete figures, lottery sales in Iowa totaled nearly \$314.8 million, already a record amount for sales of its core products (lotto games, instant-scratch games and pull-tab games) with a month still to go in FY 2013. The lottery's previous sales record from all products of \$339.5 million was set back in FY 2006.

Proceeds to state causes, meanwhile, totaled more than \$80.4 million through the end of May, which means the lottery will achieve the highest proceeds total in its 28-year history by the end of the fiscal year. Lottery proceeds to the Iowa Veterans Trust Fund in particular totaled more than \$2 million through the end of May, meaning that the lottery has met or exceeded its annual proceeds goal for veterans' causes for a fifth straight year.

Prizes to lottery players in Iowa also will set a record in FY 2013. Through the end of May, lottery players had won more than \$186 million in prizes for the year, already a record amount with a month still to go.

Another significant positive financial development for the lottery in FY 2013 is that it paid off the revenue bonds it had issued in 2004 to buy its headquarters building in Des Moines and the vending machines it currently has in the field to dispense tickets. The lottery's strong results for the year meant that it was able to pay off the bonds six years early. The lottery had issued \$8.8 million in revenue bonds in October 2004 with a maturity date of June 2019. However, the lottery paid off the entire remaining principal and interest of a little more than \$1 million on June 5.

Much of the lottery's success this year has come from strong results in Powerball, which is having an incredible year after its jackpot twice reached game-record amounts in FY 2013; and instant-scratch

games, the first lottery product sold in Iowa and always one of the lottery's leading categories, with sales from those games up more than 7 percent for the year.

Lottery products remain today what they have always been: an affordable, local entertainment option. And, while consumers may have cut back on larger entertainment expenditures, lottery products are something that is still available for just a dollar or two in local areas.

The lottery continues to evaluate potential impact on its sales from several factors, including continued high fuel prices and the rise of Internet gaming in other jurisdictions, and will keep your committees apprised of significant developments. And as always, we are closely tracking lottery results and will provide regular updates about sales and proceeds through the state's I-3 accounting system.

Here are year-to-year comparisons of lottery sales (July-May):

	<u>FY 2013</u>	<u>FY 2012</u>
Instant-scratch games	\$186.6 million	\$174.4 million
Pick 3	\$6.3 million	\$6.2 million
Powerball	\$77.1 million	\$52.6 million
Mega Millions	\$12.4 million	\$21 million
Hot Lotto	\$10.3 million	\$9.7 million
Pick 4	\$2.8 million	\$2.6 million
Iowa's \$100,000 Cash Game	\$4.1 million	\$3.9 million
Pull-tab games	\$15 million	\$16.1 million

The lottery's latest financial performance figures are included in this report as **Attachment A**. In that attachment, you'll note that lottery sales and proceeds to the state are both running well ahead of last year's results and ahead of budget projections for the year.

FY 2014 Budget Update

In the lottery's December report to your committees, we noted that during its Sept. 27 meeting, the Iowa Lottery Board had approved the lottery's FY 2014 and FY 2015 budgets in accordance with current state budgeting guidelines. As we stated at that time, the lottery remains optimistic that our publicly stated goal of providing at least \$60 million in annual proceeds to state causes will be attainable over the coming years. (This goal is based on the highest core-product proceeds amount raised during the lottery's first 25 years.)

The Lottery Board approved budget amendments for FY 2014 during its June 28 meeting. Those amendments reflect salary adjustments approved during the 2013 legislative session; elimination of the lottery's annual payment on revenue bonds it had issued in 2004 to buy its headquarters building in Des Moines and the vending machines it currently has in the field to dispense tickets, as those bonds were paid off in June; and an increase in the lottery's potential building costs, as issues are under consideration concerning its headquarters building, as detailed later in this report.

As part of standard procedures, the lottery's budget figures have been entered into the state's I-3 accounting system and are available for review by all interested parties. In addition, detailed updates to

the lottery's sales and budget figures are also regularly provided through the state's I-3 accounting system.

Copies of the lottery's Overall Budget and Operating Expenses for FY 2014 are both included with this report as **Attachments B** and **Attachment C**.



The members of the Lottery Board are: Chairperson Mary Junge of Cedar Rapids, a CPA and practicing tax and estate-planning attorney; Vice Chair Mike Klappholz of Cedar Rapids, a retired police chief; Deb Burnight, a certified professional facilitator and trainer from Sioux City; Herman Richter, president of The Three Sons clothing store in Milford and a co-founder of the popular and mythical University of Okoboji; Matt McDermott of West Des Moines, an attorney at a Des Moines law firm; and State Treasurer Michael Fitzgerald, who serves on the board as a nonvoting member.

Update Regarding Lottery Headquarters Building

In late 2012 as part of the Iowa Lottery's ongoing efforts to analyze its budget needs for the next five to 10 years, Lottery CEO Terry Rich asked lottery staff and the Iowa Department of Administrative Services (DAS) to review major maintenance and improvement needs at the lottery's headquarters building at 2323 Grand Ave. in Des Moines. The lottery has owned the building, which is nearly 60 years old, for almost 10 years and includes the structure's maintenance costs in its annual budgets.

Although the lottery has achieved savings by purchasing its headquarters property, the review revealed maintenance issues that need to be addressed in the near future and may involve major changes. Lottery executives continue to meet with state, city and private-sector experts to gather as much information as possible. The goal is to ultimately make the best-informed fiscal decision for the good of the state of Iowa, the lottery and the Des Moines area surrounding the headquarters building.



Reviews by two separate engineering firms (MODUS in Des Moines and KJWW in Urbandale) have concluded that in addition to other repair and replacement needs, the lottery building's HVAC system is well beyond its life expectancy. And, because major parts for the system are no longer produced, failure of the system would force the lottery to make an emergency replacement, displacing employees and possibly compromising lottery sales, which currently average nearly \$1 million per day.

Both engineering firms also concluded that the outdated design of the HVAC system is not compatible with modern equipment and necessitates a complete replacement, including asbestos abatement.

Other major maintenance needs at the building over the next five to 10 years include roof replacement, installation of energy efficient windows, tuck pointing and elimination of a water-infiltration issue in the garage/storage area.

Lottery executives continue to meet with experts to gather as much information as possible. The lottery has consulted with:

- Ben Brackett, Administrator, DAS Lease and Space Management Services
- Dave Peterson, DAS Senior Resource Manager
- Iowa Department of Management
- City of Des Moines
- The Baker Group in Des Moines regarding building infrastructure systems
- Smith Metzger Architects in Des Moines, consultants for the Ingersoll and Grand Avenue Planning Committee
- Iowa Alcohol Beverages Division regarding warehouse options.

The lottery is currently gathering 10- and 20-year pricing comparisons for three options:

- Renovation of the existing building
- Demolition of the existing building and construction of a smaller building on the same property
- Sale of 2323 Grand Avenue and lease of office space elsewhere.

The Lottery Board discussed the issue at its meeting on June 28 and we will continue to provide updates as developments warrant. Should a decision be made to construct a new building, prior approval would be required from the Executive Council of Iowa and the lottery would provide written notice to the legislative Government Oversight Committees.

Latest Big Lottery Winners In Iowa



With the Iowa Lottery achieving record sales in FY 2013, players also have won a record amount in prizes, including the Powerball jackpot claimed in October by a Bondurant couple. Two of the other biggest lottery prizes won in Iowa this fiscal year also were in the Powerball game.

In March, a Mahaska County man won a \$2 million Powerball prize with a ticket he bought while on his way to his mother's birthday party. Michael Lally of Barnes City matched the first five numbers in the March 23 Powerball drawing to initially win a \$1 million prize, but because he had added the Power

Play option to his ticket, his winnings were multiplied to \$2 million. Lally, 38, who works for a construction company, said he will use part of his winnings to help pay for his son's college education and he'll put a lot of it away for retirement.

And this month, a Decorah grandfather also claimed a \$2 million prize he'd won on a Powerball ticket with the Power Play option added. Don Johnson, 80, won his big prize in the June 22 drawing. He said that his wife of nearly 50 years, Shirley, is in a nursing home and his winnings can help pay for her care.

Internet Gambling

Internet gaming remains an ongoing topic of discussion in Congress and we continue to monitor developments on the federal level to analyze their potential impact on Iowa. You'll recall that the National Governor's Association, National Conference of State Legislatures, and National Council of Legislators from Gaming States all stepped forward last winter to emphasize that the federal government should not infringe on states' rights to implement and regulate Internet gaming within their own borders. And, although several proposals were introduced, no federal Internet gaming legislation was passed during the last Congressional session following those statements by state officials.



However, new federal legislation on the topic has been introduced this month. The proposal from U.S. Rep. Peter King, R-New York, would legalize Internet wagering and establish federal licensing and regulation under the U.S. Secretary of the Treasury.

Iowa Lottery officials traveled to Washington in December to lend our voices to those of the state elected officials who had spoken out. We stated at the time and continue to stress that individual states are best equipped to respond to their citizens' unique local preferences and decide what, if any, intrastate gaming should occur within their jurisdictions.

The Iowa Lottery has the authority to conduct Internet gaming and continues to study the issue, remaining cognizant of the fact that there would be a negative impact on proceeds to state causes if it does not adapt to player expectations for convenience and use of technology.

As stated before, we will provide updates to your committees and the Legislature as a whole about changes that could be involved in Iowa and the impact such issues could have on the state budget. We also believe it is crucial to continue efforts to ensure that the state protects its rights and resources in this matter.

We continue to offer ourselves as a business analyst to offer outside perspective, advice and revenue projections in these discussions.

IOWA LOTTERY
PERFORMANCE MEASURES
FY 2013

Attachment A

Month		JUL	AUG	SEP	OCT	NOV	DEC	JAN	FEB	MAR	APR	MAY			JUN
Gross Sales	Budget '13	20,704,712	23,236,949	21,008,030	21,964,053	22,422,595	23,240,177	23,369,824	24,166,499	26,112,372	24,460,279	24,080,068			22,334,442
	Actual '11	20,683,463	20,526,880	20,268,736	20,707,755	22,414,149	23,638,991	23,866,645	22,592,711	27,156,908	24,150,580	22,962,332			22,421,899
	Actual '12	21,873,877	24,265,848	21,821,737	24,435,865	25,093,494	26,243,111	25,715,692	30,212,168	34,836,028	25,760,263	26,307,787			24,285,855
	Actual '13	24,002,158	27,670,234	23,898,937	25,478,715	35,880,677	25,193,904	26,916,821	28,760,205	33,398,754	27,742,685	35,815,945			-
Prize Expense	Budget '13	12,225,406	13,720,606	12,404,507	12,969,005	13,239,758	13,722,512	13,799,064	14,269,472	15,418,442	14,442,939	14,218,438	59.05% 1)		13,187,707
	Actual '11	12,779,039	11,692,728	11,763,446	12,293,596	12,390,886	14,042,187	13,741,084	14,281,690	15,042,753	13,796,588	13,991,657	60.93% 2)		13,145,432
	Actual '12	12,753,428	13,913,842	12,543,873	14,418,330	13,955,317	16,548,952	15,632,293	17,991,110	19,681,217	15,101,762	15,850,810	60.25% 3)		14,051,517
	Actual '13	14,725,708	15,978,048	14,152,073	14,520,050	20,300,550	15,702,205	16,369,611	17,429,155	20,337,318	16,343,726	20,154,706	56.27% 4)		-
Operating Expenses	Budget '13	458,823	982,362	982,362	1,432,779	849,140	982,362	988,706	988,706	988,706	1,442,295	855,484			1,640,924
	Actual '11	539,097	693,153	884,831	807,776	1,184,565	703,967	828,828	936,391	850,695	888,354	1,287,987			1,548,869
	Actual '12	460,879	794,576	991,760	874,688	1,261,482	757,874	882,297	883,113	949,752	878,951	1,376,977			1,919,910
	Actual '13	523,449	891,820	958,942	1,344,045	772,498	877,989	960,065	974,427	917,908	1,316,432	768,753			-
Proceeds to General Fund	Budget '13	4,898,370	5,030,028	4,453,312	4,250,259	4,952,542	5,030,864	5,058,065	5,264,198	5,767,679	4,886,623	5,375,057			4,137,949
	Actual '11	4,714,318	5,198,524	4,295,667	5,010,008	6,255,411	5,606,161	6,208,866	4,335,482	7,234,879	6,253,580	4,814,963			4,968,521
	Actual '12	5,684,111	6,081,167	5,029,059	5,818,860	7,365,377	5,345,966	5,759,711	7,373,869	9,782,829	6,894,379	5,829,479			5,047,647
	Actual '13	5,310,624	6,687,662	6,055,941	7,105,024	10,310,506	4,651,853	6,409,126	6,499,139	8,023,688	6,934,843	10,417,377			-
Proceeds to Veterans Trust	Budget '13	91,838	462,261	333,090	181,235	149,349	144,787	207,474	316,167	411,416	219,105	160,997			122,281
	Actual '11	131,645	382,640	441,669	251,116	208,123	203,448	184,063	267,748	472,319	229,155	180,589			152,856
	Actual '12	57,594	350,656	391,066	165,122	128,253	155,046	321,611	406,376	267,787	248,021	149,725			78,236
	Actual '13	268,863	450,192	101,538	69,313	69,101	98,944	253,973	423,787	108,004	104,807	93,004			-
Total Proceeds	Budget '13	4,990,208	5,492,289	4,786,402	4,431,494	5,101,891	5,175,651	5,265,539	5,580,365	6,179,095	5,105,728	5,536,054			4,260,230
	Actual '11	4,845,963	5,581,164	4,737,336	5,261,124	6,463,534	5,809,609	6,392,929	4,603,230	7,707,198	6,482,735	4,995,552			5,121,377
	Actual '12	5,741,705	6,431,823	5,420,125	5,983,982	7,493,630	5,501,012	6,081,322	7,780,245	10,050,616	7,142,400	5,979,204			5,125,883
	Actual '13	5,579,487	7,137,854	6,157,479	7,174,337	10,379,607	4,750,797	6,663,099	6,922,926	8,131,692	7,039,650	10,510,381			-
YEAR TO DATE															
Gross Sales	Budget '13	20,704,712	43,941,661	64,949,691	86,913,744	109,336,339	132,576,516	155,946,340	180,112,839	206,225,211	230,685,490	254,765,558			277,100,000
	Actual '11	20,683,463	41,210,343	61,479,079	82,186,834	104,600,983	128,239,974	152,106,619	174,699,328	201,856,234	226,006,812	248,969,142	26.42% 5)		271,391,047
	Actual '12	21,873,877	46,139,725	67,961,462	92,397,327	117,490,821	143,733,932	169,449,624	199,661,792	234,497,820	260,258,083	286,565,870	9.84% 6)		310,851,725
	Actual '13	24,002,158	51,672,392	75,571,329	101,050,044	136,930,721	162,124,625	189,041,446	217,801,651	251,200,405	278,943,090	314,759,035	23.55% 7)		
Prize Expense	Budget '13	12,225,406	25,946,012	38,350,519	51,319,524	64,559,282	78,281,794	92,080,858	106,350,330	121,768,772	136,211,711	150,430,149	59.05% 1)		163,617,856
	Actual '11	12,779,039	24,471,767	36,235,213	48,528,809	60,919,695	74,961,882	88,702,966	102,984,649	118,027,395	131,823,976	145,815,626	58.57% 2)		158,961,078
	Actual '12	12,753,428	26,667,270	39,211,143	53,629,473	67,584,790	84,133,742	99,766,035	117,757,145	137,438,362	152,540,124	168,390,934	58.76% 3)		182,442,447
	Actual '13	14,725,708	30,703,756	44,855,829	59,375,879	79,676,429	95,378,634	111,748,245	129,177,400	149,514,718	165,858,444	186,013,150	59.10% 4)		
Operating Expenses	Budget '13	458,823	1,441,185	2,423,547	3,856,326	4,705,466	5,687,828	6,676,534	7,665,240	8,653,946	10,096,241	10,951,725			12,592,649
	Actual '11	539,097	1,232,250	2,117,081	2,924,857	4,109,422	4,813,389	5,642,217	6,578,610	7,429,307	8,317,663	9,605,652			11,154,514
	Actual '12	460,879	1,255,455	2,247,215	3,121,903	4,383,385	5,141,259	6,023,556	6,906,669	7,856,421	8,735,372	10,112,349			12,032,258
	Actual '13	523,449	1,415,269	2,374,211	3,718,256	4,490,754	5,368,743	6,328,808	7,303,235	8,221,143	9,537,575	10,306,328			
Proceeds to General Fund	Budget '13	4,898,370	9,928,398	14,381,710	18,631,969	23,584,511	28,615,375	33,673,440	38,937,638	44,705,317	49,591,940	54,966,997			59,104,946
	Actual '11	4,714,318	9,912,842	14,208,509	19,218,517	25,473,928	31,080,089	37,288,955	41,624,438	48,859,318	55,112,899	59,927,863			64,896,382
	Actual '12	5,684,111	11,765,278	16,794,337	22,613,197	29,978,574	35,324,540	41,084,251	48,458,120	58,240,949	65,135,328	70,964,807			76,012,455
	Actual '13	5,310,624	11,998,286	18,054,227	25,159,251	35,469,757	40,121,610	46,530,736	53,029,875	61,053,563	67,988,406	78,405,783			
Proceeds to Veterans Trust	Budget '13	91,838	554,099	887,189	1,068,424	1,217,773	1,362,560	1,570,034	1,886,201	2,297,617	2,516,722	2,677,719			2,800,000
	Actual '11	131,645	514,285	955,954	1,207,070	1,415,193	1,618,641	1,802,704	2,070,452	2,542,771	2,771,926	2,952,515			3,105,371
	Actual '12	57,594	408,250	799,316	964,438	1,092,691	1,247,737	1,569,348	1,975,724	2,243,511	2,491,532	2,641,257			2,719,494
	Actual '13	268,863	719,055	820,593	889,906	959,007	1,057,951	1,311,924	1,735,711	1,843,715	1,948,522	2,041,526			
Total Proceeds	Budget '13	4,990,208	10,482,497	15,268,899	19,700,393	24,802,284	29,977,935	35,243,474	40,823,839	47,002,934	52,108,662	57,644,716			61,904,946
	Actual '11	4,845,963	10,427,127	15,164,463	20,425,587	26,889,121	32,698,730	39,091,659	43,694,890	51,402,089	57,884,825	62,880,378	27.94% 5)		68,001,753
	Actual '12	5,741,705	12,173,528	17,593,653	23,577,635	31,071,265	36,572,277	42,653,559	50,433,844	60,484,460	67,626,860	73,606,064	9.29% 6)		78,731,949
	Actual '13	5,579,487	12,717,341	18,874,820	26,049,157	36,428,764	41,179,561	47,842,660	54,765,586	62,897,278	69,936,928	80,447,309	39.56% 7)		

- 1) Budget FY13 Prize Payout
- 2) Actual FY11 Prize Payout
- 3) Actual FY12 Prize Payout
- 4) Actual FY13 Prize Payout
- 5) Actual FY13 compared to Actual FY11
- 6) Actual FY13 compared to Actual FY12
- 7) Actual FY13 compared to Budget FY13

Budget for Lottery Fund

Attachment B

	FY 2012 ACTUAL	FY 2013 BOARD APPROVED FINAL BUDGET	FY 2014 BOARD APPROVED PRELIMINARY BUDGET	FY 2014 BOARD APPROVED FINAL BUDGET
<u>Resources</u>				
Lottery sales	310,851,725	277,100,000	281,000,000	293,000,000
Interest income	105,755	500,000	500,000	500,000
Application fees	4,075	5,000	5,000	5,000
Other	212,884	5,000	5,000	5,000
Total Resources	311,174,439	277,610,000	281,510,000	293,510,000
<u>Expenses and Change in Net Assets</u>				
Prizes	182,442,447	163,617,855	165,430,394	171,872,697
Retailer compensation	20,125,497	17,648,025	18,193,075	18,969,721
Advertising production and media purchases	6,603,456	11,084,000	11,240,000	11,720,000
Retailer Lottery system/Terminal Communications	6,213,722	6,392,184	6,474,240	6,827,940
Instant/Pull-tab ticket expense & machine maintenance	3,705,428	3,622,000	4,085,000	4,085,000
Terminal equipment/Ticket dispensers/Vending machines	213,216	200,000	250,000	250,000
Courier delivery of instant tickets	108,581	455,000	535,000	535,000
Interest expense (ITVM/PTVM/Building)	39,134	45,000	32,840	-
Lottery operating expense	11,979,788	12,592,649	13,015,308	13,503,394
Increase (decrease) in net assets; building	1,011,221	48,341	48,341	3,448,341
Total Expenses and Change in Net Assets	232,442,490	215,705,054	219,304,198	231,212,093
<u>Proceeds</u>				
Proceeds Transfer to General Fund	76,012,455	59,104,946	59,405,802	59,497,907
Proceeds Transfer to Veterans Trust Fund	2,719,494	2,800,000	2,800,000	2,800,000
Total Proceeds Transfers	78,731,949	61,904,946	62,205,802	62,297,907
Total Expenses and Proceeds	311,174,439	277,610,000	281,510,000	293,510,000

Lottery Operations - Budget Detail

Attachment C

	FY 2012 ACTUAL	FY 2013 BOARD APPROVED FINAL BUDGET	FY 2014 BOARD APPROVED PRELIMINARY BUDGET	FY 2014 BOARD APPROVED FINAL BUDGET
Administrative payroll	9,120,063	9,915,649	9,915,649	10,027,895 *
Travel	451,040	443,000	495,000	495,000
Supplies	116,163	105,000	125,000	125,000
Printing	11,022	15,000	16,000	16,000
Postage	6,238	6,000	6,500	6,500
Communications	124,769	175,000	160,000	160,000
Rentals	290,595	300,000	305,000	328,000
Utilities	97,579	105,000	105,000	105,000
Professional fees	161,225	135,000	170,000	495,000
Outside services and repair	340,749	400,000	400,000	427,840
Data processing	50,320	50,000	55,000	55,000
Equipment	500,015	170,000	430,500	430,500
Reimbursement to state agencies	433,436	450,000	475,000	475,000
Depreciation	173,611	223,000	251,659	251,659
Other expenses	102,963	100,000	105,000	105,000
Total operating expenses	\$ 11,979,788	\$ 12,592,649	\$ 13,015,308	\$ 13,503,394

* 2014 Proposed Final Budget for "Administrative Payroll" includes salary and benefit cost increases (per DOM projections).